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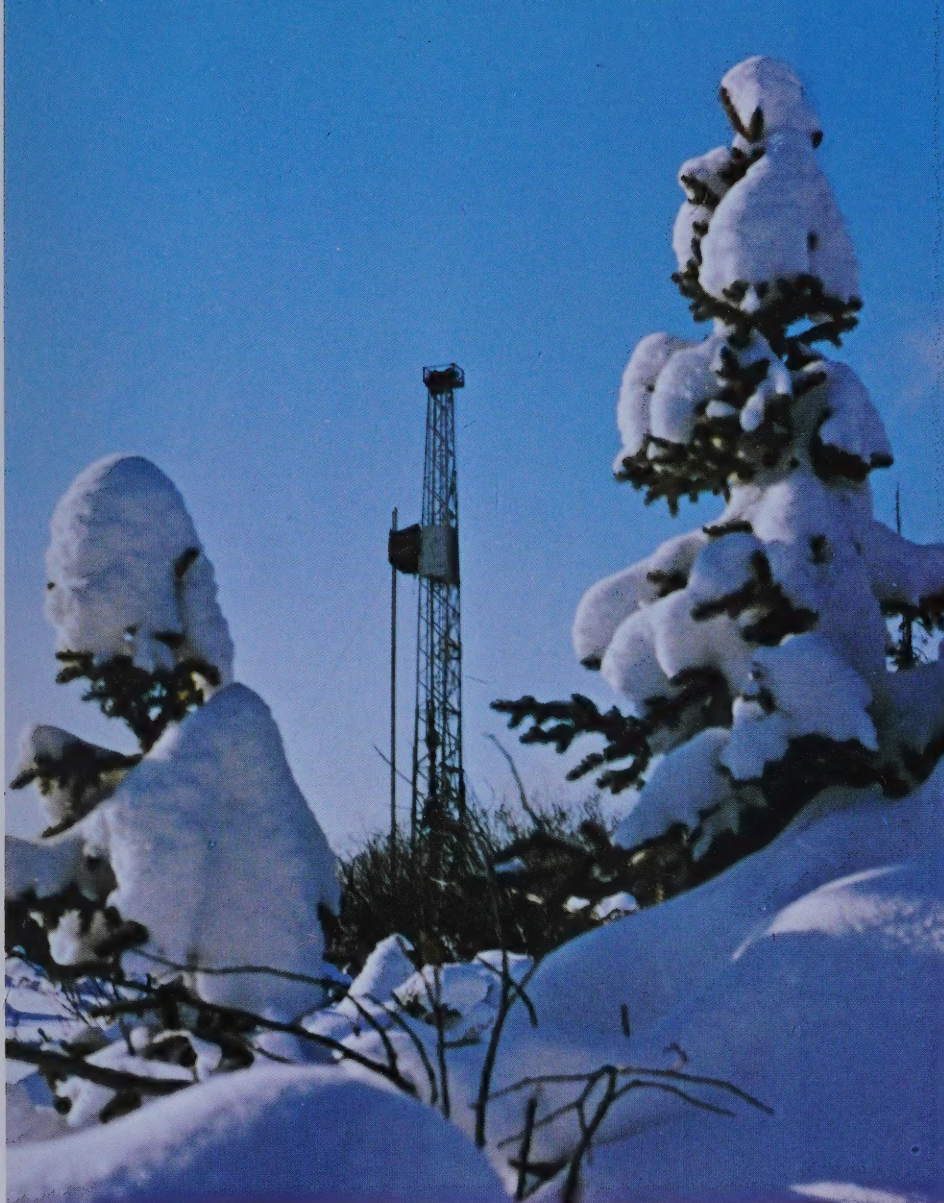
## Directors' Advisory Council

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WM. L. HOLLOWAY, San Francisco  
Member law firm, Morrison, Foerster,  
Holloway, Clinton & Clark, General Counsel

LOYD WRIGHT, Los Angeles  
Senior Partner, Wright, Rodi, Wright, Tolton & Van Zyl

The cover painting depicts the Aurora Borealis, or Northern Lights. They occur in an infinite variety of forms across the northern reaches of the North American Continent, an area in which your Company continues to take an increasing interest.



Heavy snow blankets a well site in Northeast British Columbia.

## FINANCIAL

	1969	1968
Total revenues . . . . .	\$44,336,521	\$39,564,402
Net income		
Total . . . . .	4,381,603	3,091,214
Per common share, after preferred dividends . .	.44	.33
Working capital . . . . .	9,243,375	10,241,549
Shareholders' equity . . . . .	57,988,619	42,807,978
Total assets . . . . .	80,007,755	75,087,478

## OPERATING

Crude oil and natural gas liquids production, barrels per day . . . . .	9,706	9,476
Natural gas sales, Mcf per day . . . . .	40,053	37,157

## Financial and Operating Highlights



## From the President



1969 was by far your Company's best year. Gross revenues and net income reached all-time record levels and excellent results were achieved in virtually every financial category.

Gross Revenues were up 12.1% to \$44.34 million (1968—\$39.56 million)

Net Income was up 41.7% to \$4.38 million (1968—\$3.09 million)

Net Income per Common Share was up 33.3% to \$.44 (1968—\$.33)

In addition, compared to exploratory land holdings (exclusive of its U.S. and Canadian Exploration Programs with other parties) of approximately 623,465 net acres at the end of 1968, Reserve at the end of 1969 held a total of 24,612,216 net exploratory acres. This enlarged acreage holding significantly increases your Company's exposure to discovery by exploration.

Net earnings included a gain on the sale of 1.6 million acres of prospecting permits in Canada for \$1,029,740, net of taxes. This gain accounted for \$.12 of the total net income per common share. At year end working capital was at a satisfactory level of \$9,243,375. Cash flow for the year reached a record high of \$7,292,676.

1969 was also one of Reserve's most active years in respect to acquisitions—and possibly the most rewarding over the long term. In September Reserve acquired Mission Oil Development Ltd. of Alberta, Canada in exchange for 335,000 shares of Reserve com-

mon stock and warrants to purchase 100,000 shares of Reserve common at \$15 per share. Also in September, Pheasant Exploration Ltd. and Pheasant Petroleum Ltd. were acquired, in exchange for 40,000 shares of Reserve common. Through these transactions Reserve obtained ownership of oil and gas exploration permits, petroleum and natural gas reservations and oil and gas leases comprising working interests in 27.7 million gross acres and 26.3 million net acres in several of the principal sedimentary basins throughout Canada. These properties included approximately 11.1 million net acres in the Arctic Islands; 7.9 million in the Yukon and Northwest Territories and 6 million in the East Coast Canadian offshore area, together with lesser holdings in Manitoba, Saskatchewan, Alberta, the Gaspé Peninsula, Bowser Basin and offshore Western Canada. Also acquired were royalty holdings in 4.4 million gross or 113,849 net royalty acres in Western Canada, together with certain other mineral interests. A recent oil discovery by Imperial Oil Ltd. in the Mackenzie Delta area of the Northwest Territories and gas and condensate discovered by Pan Arctic Drake Point wells in the Arctic Islands indicate the enormous potential of these far north sedimentary basins.

A number of possibilities to provide for the exploration of these major holdings are under consideration by your company. Substantial work guarantees are re-

quired in order to hold these lands and discussions are in progress with a view to obtaining adequate funds for this purpose. With exploration efforts in the Canadian sedimentary basins now rapidly increasing by all segments of the oil and gas industry, particularly in the Arctic Islands, these acquired holdings are located in areas where every indication points to accelerated commitments of funds directed to the discovery of oil and gas and other minerals.

In April 1969, the name of Reserve's Canadian subsidiary, Fargo Oils Ltd., was changed to Canadian Reserve Oil and Gas Ltd. in order to achieve increased recognition of Reserve's total operations.

Through another acquisition Reserve became a more integrated oil and gas company. In August, the assets and business of Mohawk Petroleum Corporation, one of California's oldest independent refining and marketing companies, were consolidated into Reserve. This was accomplished by the issuance of 173,790 shares of a new Series D 5½% cumulative convertible preferred stock and 599,924 shares of common. The principal refining and marketing assets of Mohawk include its Bakersfield Refinery, which has been in operation for 38 years; 183 retail outlets, comprising 134 service stations featuring the Mohawk brand and 49 rebrand sales outlets; and approximately 110 additional installations in automobile agencies,

garages and fleet centers. Through this entry into the largest market for motor gasoline and related products in the nation, a substantial contribution to your company's revenues and business is indicated. The future in this respect depends to a degree upon the future of the oil import program. It now appears that near-term changes in this program are unlikely.

Through Mohawk, Reserve also acquired over 30 oil and gas producing properties, principally in California, Texas and Wyoming and 134,138 net acres of exploratory mineral leases in the United States and Canada, together with approximately \$2 million in liquid assets and 32 fee properties. In September Malcolm McDuffie was appointed President of Mohawk Petroleum Corporation, Inc., a new company, which will operate as a wholly-owned subsidiary of Reserve and continue the Mohawk brand name which has been well known in California for many years.

During 1969 your company also moved ahead in its two major exploration programs. In August, the Reserve-Halbouty Exploration Program in Canada was extended for another year with an additional exploratory commitment of \$1,500,000, of which \$1,200,000 will be put up by the Program's unaffiliated corporate participant. The Halbouty-Reserve U.S. Exploration Program was also extended for another year, in September. An additional \$2 million in exploratory funds was committed by the unaffiliated corporate participant associated with Halbouty and Reserve in this Program. Discoveries were made during 1969 under both of these programs. Details of the discoveries and development activities, plus plans for additional work in 1970 are described in the text of this report.

An important sour gas discovery was made on Company-owned land in the Lone Pine Creek area of Southern Alberta. This is also

described in the following text material.

Production and sales of oil, gas and sulphur for the year were favorable. Daily average production of oil and natural gas liquids increased 2.4% to a total of 9,706 barrels per day; and natural gas sales averaged 40,053 Mcf per day, showing a 7.8% increase over the prior year. 34,137 long tons of sulphur were sold from the East Crossfield, Alberta plant resulting in \$642,396 (U.S.) of net revenues after royalty. This is a 90% increase over proceeds realized in the second half of 1968 after sales commenced. Sulphur prices continued to decline, but operations were maintained on a profitable basis.

Despite increasingly severe monetary conditions as the year passed, land sales by the Apple Valley Ranchos Division were maintained at a satisfactory level. Total sales, including both properties owned by the company and owned by others, aggregated \$2.6 million, compared to \$3.3 million in 1968. Subdivision planning and construction work were maintained at a high level and a favorable lot inventory has been developed.

The \$25 million Cedar Springs Dam, which will impound the water for Silverwood Lake, is 45% complete. This facility is located immediately to the south of Apple Valley and is a part of the Feather River Water Project, and will contain a 4,400-acre recreational development. A new \$2½ million airport was completed just north of Roy Rogers' Apple Valley Inn.

The major expansion program at the Hanford Fertilizer Plant has been completed except for equipment installation in the phosphoric acid unit and a material design problem in the fluid bed granulation unit. The fluid bed unit, which is of an experimental design, has caused substantial difficulty and additional design modifications are now being made in an effort to make this unit, and the entire

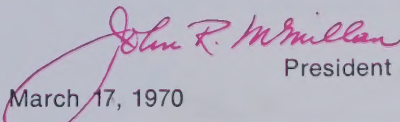
plant, fully operative. Dry fertilizer products are being manufactured in the new plant without this facility, but only at about one-third of capacity. Additional productive capacity must be achieved in the new plant before profitable operations can be realized. Every effort is being made to reach this goal.

On June 13, 1969 Reserve called its convertible subordinated debentures for redemption and fixed July 16 as the effective redemption date. Of the original issue of \$14 million in debentures, \$2,330,000 had been converted into common stock prior to the call. Out of the remaining \$11,670,000 of these bonds \$11,651,000 were converted prior to the redemption date and the remaining \$19,000 were redeemed. Through this call for redemption and the debenture holders' election to convert, the company's debt service was reduced by \$760,000 per year.

During the first quarter of 1970 an important step was taken to accelerate and promote the company's exploration plans in Canada. On February 24, Mission Oil Development Ltd. and the two Pheasant companies were consolidated into Canadian Reserve to form an amalgamated company under the laws of the Province of Alberta. This move will result in increased efficiency and economy and, more important, will coordinate and advance the administration of all of the company's Canadian exploration and development operations under a combined management.

1969 was clearly a year which established a greater potential for future growth than any prior year. No opportunity will be overlooked for realization of that potential. With the groundwork that has now been completed, the prospects for continued achievement are favorable.

For the Board of Directors

  
President  
March 17, 1970

# Exploratory Land Holdings in Canada and Alaska

In August of 1969 Reserve, through its wholly-owned subsidiary Canadian Reserve Oil and Gas Ltd., held substantial interests (shown in green on the map) in the western areas of Canada and in the Arctic Islands.

With the acquisition of Mission Development Ltd., Pheasant Exploration Ltd., and Pheasant Petroleum Ltd., in September 1969, these holdings were greatly increased by the addition of more than 26 million net acres (shown in red on the map). The company is now well represented in the principal areas of major exploratory activity in Canada, ranging from the West Coast offshore, the Yukon and the Northwest Territories and the Arctic Islands to both onshore and offshore eastern Canada.

It is anticipated that 30 to 35 exploratory wells will be drilled in the next 2-3 year period in the Arctic Islands. During that same period the petroleum industry will be conducting a massive exploration effort in the Northwest Territories. 15 to 20 exploratory wells are reportedly planned in the Gulf of St. Lawrence and eastern Canadian offshore area.

Although complicated problems of exploration, operation, transportation and marketing exist in many of these regions, all signs point to very heavy commitments of funds directed to the discovery of oil, gas and other minerals and to the solution of such problems.



## LEGEND

- Canadian Reserve Major Acreage Holdings
- Mission Oil Development Acquired Acreage
- /// Sedimentary Basins  
(Potential Oil and Gas Areas)

CANADA AND ALASKA ACREAGE AND PRODUCING WELLS  
as of December 31, 1969

	Gross Acreage	Undeveloped Acreage		Developed Acreage		Oil and Gas Wells	
		Gross	Net	Gross	Net	Gross	Net
British Columbia .....	1,204,811	1,044,848	436,011	159,963	38,611	83	16.93
Alberta .....	944,022	892,713	136,524	51,309	20,957	132	41.50
Saskatchewan .....	1,061,649	1,016,470	74,053	45,179	10,673	293	239.44
Manitoba .....	216,519	213,581	129,801	2,938	1,515	49	23.10
Northwest Territories ..	8,861,692	8,861,692	5,446,689	—	—	—	—
Yukon Territories .....	2,241,860	2,241,860	1,636,369	—	—	—	—
Arctic Islands .....	12,921,791	12,921,791	10,296,351	—	—	—	—
East Coast .....	6,054,289	6,054,289	6,054,289	—	—	—	—
West Coast .....	294,698	294,698	294,698	—	—	—	—
Italian Adriatic .....	30,000	30,000	96	—	—	—	—
Quebec .....	265,000	265,000	198,750	—	—	—	—
Alaska .....	52,166	52,006	9,901	160	30	1	.11
	34,148,497	33,888,948	24,713,532	259,549	71,786	558	321.08

NOTE: The above includes all acreage holdings and wells owned by Reserve, including Reserve's interest in the R.H. Program, and Canadian subsidiaries. Oil and gas wells include all producing wells and wells capable of production and wells which were contributed to units.



Top left—Winter sunset at a drilling rig in Northeast British Columbia.  
 Top right—Floor of drilling rig on exploratory well near Clark Lake in Northeast British Columbia.

Center left—A Company rig seeks new oil reserves in the snowy reaches of North Central Alberta's Swan Hills area.



Center right—Living quarters for drilling crews are compact yet provide modern comforts in the extreme cold Canadian winter.

Bottom left—View of drilling rig in Northeast British Columbia.

Bottom right—Sheets of ice cover the shaker mechanism on a drilling well in Northeast British Columbia.



# Exploration, Development and Operations

**CANADIAN RESERVE OIL AND GAS LTD.** During September 1969, Reserve acquired all of the outstanding shares of three Alberta, Canada corporations: Mission Oil Development Ltd., Pheasant Exploration Ltd., and Pheasant Petroleums Ltd. The acquired companies are referred to as the "Mission Group companies."

**LAND—The Mission Group Companies** As a result of the acquisition of the Mission Group companies, Reserve dramatically increased its land holdings in the principal sedimentary basins of Canada, as detailed on preceding pages.

Subsequent to the Mission Group acquisition, prospecting permits covering approximately 1,600,000 acres in the Banks Island and Yukon Territory areas were sold. The consideration for these sales amounts to \$1,489,704, net after commission. A gross overriding royalty of 3% was retained on all prospecting permits sold, except one permit of approximately 25,000 acres. During October 1969, the Mission Group agreed to the sale of its 32% interest in Italian Adriatic acreage, for approximately \$30,000 and a retained 1% gross overriding royalty.

As a result of the acquisition of the Mission Group companies, Reserve held at year-end, in its own name or through its wholly-owned subsidiaries, Canadian Reserve and the Mission Group companies, and through the Reserve-Halbouty Canadian Exploration Program, aggregate working in-

terests in 34.1 million gross acres, or 24.7 million net acres in Canada. This acreage is set out by area in the tables on page 5.

**PRODUCTION** Canadian Reserve production of crude oil and natural gas liquids averaged 5,194 barrels per day in 1969, compared with 4,895 barrels per day in 1968.

Gas sales increased to 15,243 MCF/D in 1969 from 9,968 MCF/D in 1968, for a 52.9% increase. Gas sales net to the Company's interests in the East Crossfield area in Central Alberta accounted for most of this significant increase. Net sulphur production from the East Crossfield D-1 sour gas plant, increased from 100 long tons per day in 1968 to 113 long tons per day in 1969. The Company sold 34,137 long tons of sulphur at a plant net back price of \$18.82 (U.S.) per long ton in 1969.

**DRILLING** In 1969 Canadian Reserve participated as a working interest owner in drilling 45 wells; 2 in Alberta, 4 in British Columbia and 39 in Saskatchewan. In addition, there were 9 wells drilled on farmout, carried working interest or option lands to evaluate the Company's acreage. Of the 54 wells in which the Company participated, 11 were exploratory and 43 were development wells which resulted in 40 gross (7.16 net) oil wells, 5 gross (1.11 net) gas wells and 9 gross (1.35 net) dry holes. Of the 11 exploratory wells, 7 were dry and abandoned and 4 were completed as gas wells.

**EXPLORATION AND DEVELOPMENT** Some of the more significant exploration and development activi-

ties undertaken or planned by Canadian Reserve are summarized below:

**BRITISH COLUMBIA** Canadian Reserve holds varying interests in 850,325 gross acres (269,402 net acres) in Northeast British Columbia, an area which continues as one of the most active exploration areas in Western Canada. An important exploratory well drilled was the Tenneco-operated Inga c-20-J well in which the Company owned a 10.16% interest, which encountered gas containing 39% H<sub>2</sub>S in the Inga Sand at a depth of 5,370 feet. The well blew out upon encountering the Inga Sand development, which ultimately resulted in the operator's decision to plug and abandon the well. A replacement, plus additional wells, will be required in this area to develop the Inga Sand sour gas reservoir.

Water injection operations were initiated in the Inga Unit No. 1 in northeast British Columbia in June, 1969. The Company owns an 8.1% working interest in the Unit which encompasses 12,640 acres developed by 41 wells. The Inga Sand reservoir, at a depth of 5,300 feet, has been granted a pool allowable increase, as a result of secondary recovery operations, from 4,200 barrels per day to 7,250 barrels per day. The new allowable results in an increase of 240 barrels per day to the Company's Unit interest.

Joint engineering studies completed in 1969 of the Inga Sand gas cap area, located immediately north and adjacent to the Inga

East Crossfield Sulphur Plant:

Top—Bulk sulphur awaits shipment.  
Center, left and right—Structural details at the plant.

Bottom left—Sulphur in liquid form is sprayed onto the drying beds.

Bottom right—A technician makes an adjustment in the complex controls at the plant.



## Exploration, Development and Operations, continued

Sand No. 1 Unit, indicates recoverable proved and probable gas reserves in the order of 130 billion cubic feet which can be produced without affecting ultimate recovery from the Inga Sand oil reservoir. As a result of the engineering studies, plans are currently in progress to unitize the gas cap area, in which the Company is expected to own an approximate 8% interest, and to drill the necessary producing gas wells and install gathering facilities to initiate gas sales from the reservoir in late 1970.

**ALBERTA** During 1969, the Company continued to place emphasis on the search for and production of gas reserves in the Alberta basin.

During the year, the combined processing facilities of the East Crossfield Elkton and D-1 Units produced at a rate of 89 MMCF/D. The Company owns a 10.9% interest in the combined gas processing facilities, 8.16% of the D-1 Unit and sulphur recovery facilities and a 13.65% interest in the Elkton Unit and liquid recovery facilities which will be increased to approximately 16% following inclusion in the Unit, in 1970, of proven reserves underlying a 640-acre tract in which the Company owns a 36% interest.

The most significant development well drilled by Canadian Reserve in 1969 was in the area immediately east of the East Crossfield D-1 Sour Gas Unit and south of the Lone Pine Creek D-1 Sour Gas Unit, where the Company

owns a 100% interest in 9,111 acres. The Company's 7-28 well, drilled on a 1,920-acre contiguous block of the Company's land, encountered 45 feet of net D-1 sour gas pay at a depth of 8,010 feet, and was completed with an Absolute Open Flow potential of 17.6 MMCF/D. Additional drilling is planned by the Company and other operators in the immediate area in 1970 to further delineate the Lone Pine Creek D-1 sour gas reservoir.

Canadian Reserve owns a 50% interest in 12,160 gross acres in the Innisfail area located some 50 miles north of Calgary, Alberta. The Company is currently participating in an extensive seismic survey in search of Woodbend Reefs of Devonian age with its 50% working interest partner. Any anomalies delineated by the current seismic surveys will be scheduled for drilling in 1970.

**SASKATCHEWAN** During 1969 Canadian Reserve continued to place emphasis on increasing reserves and production performance of its properties in the heavy oil producing area of Lloydminster, where the Company at year-end owned interests in 164 gross (149 net) oil wells. Thirty-nine of the 43 development wells drilled in which the Company participated, were in this heavy crude oil producing area.

The South Epping Unit, formed in February 1966, in which the Company owns a 52% interest, contains 4,080 acres and is developed by 102 wells. Water in-

jection was initiated in the north one-half of this unit in August 1966 with water injection operations expanded into the south one-half of the unit in March 1969. Crude oil production from the unit in 1969 averaged 2,985 barrels per day compared to 2,306 barrels per day in 1968 for a 29.5% increase. Additional producing rate increases are expected in 1970 as response is obtained to water injection in the south one-half of the unit.

Effective June 1, 1969 the Company committed ten wholly-owned wells in the South Aberfeldy Unit for the purpose of conducting unitized secondary recovery operations by water injection into the Sparky Sand Reservoir at a depth of 1,750 feet. The Company owns an 11.96% unit interest in this unit.

The Company in 1969 drilled ten stratigraphic tests in an exploratory program in search of new heavy oil reserves. The program was successful, resulting in three tests which encountered commercial thicknesses of oil sands. New lands were acquired and exploration and development drilling will be conducted in 1970 to develop and delineate the indicated reservoirs.

**NORTHWEST TERRITORIES — ARCTIC ISLANDS** Canadian Reserve at year-end, held interests in 24.0 million acres in the Arctic Islands, Northwest Territories, and Yukon Territory of Northern Canada, an area where widespread geophysical, exploration and drilling activ-

## Exploration, Development and Operations, continued

ity is currently taking place. A recent discovery by Imperial Oil Ltd. at Atkinson Point in the MacKenzie Delta area of the Northwest Territories indicates a potential of substantial reserves in the sedimentary basins of these far northern areas. This discovery is expected to substantially increase the tempo of exploration.

Canadian Reserve in 1967 committed interests ranging from 25 to 50% in approximately 400,000 acres in the Arctic Islands to the Panarctic Oils, Ltd. Arctic Exploration Program. At year-end this Program was in full progress. Three wells had been drilled and abandoned and two wells were currently drilling. The Panarctic Drake Point #1 well located on Melville Island, encountered and tested two gas zones at reported depths of 3,750 and 4,650 feet, and a third zone below 10,000 feet, which had not been tested. Continued exploration and drilling is assured in the Arctic Islands over the next two-year period by Panarctic and King Resources. Other acreage holders within the Arctic Islands area are expected to initiate gravimeter, aeromagnetic and seismic reconnaissance programs in efforts to delineate drillable features.

In the Southern Plains area of the Northwest Territories, the Company is conducting during the 1969-70 winter season an extensive gravimeter, magnetometer and seismic survey on a 2.6 million acre block. The cost of this exploration program will be paid by another company in order

to earn a 50% interest in the wholly-owned Company lands, which are in an area of Middle Devonian Reef possibilities. In excess of 25 wells have been announced for drilling during the 1969-70 winter season to the south of the Company's holdings.

At January 1, 1969 the aggregate amount of Canadian Reserve production loans outstanding, which are repaid out of the proceeds of production, amounted to \$5,044,995 (U.S.) subject to provisions for interest ranging from 6½ to 8½% per annum accruing monthly on the unrecovered balance. Production loan applications during 1969 totaled \$1.66 million to principal and \$308,000 to interest, resulting in an aggregate year-end production loan principal balance of \$3.38 million.

**MID-CONTINENT DIVISION** Reserve produced and sold an average of 2,886 barrels of crude oil, condensate and natural gas liquids per day and 20,253 Mcf of gas per day from its Mid-Continent properties in 1969, net to the Company's interest before application to production payments. The major portion of the Company's properties located in this region was purchased in 1963 subject to reserved production payments in the amount of \$22.3 million along with amounts equivalent to interest at rates ranging from 5½ to 6¾%. Through the end of 1969, Reserve has applied a total of \$14.62 million to principal and \$5.78 million to interest on the production payments resulting in an aggregate year-end production

payment principal balance of \$7.68 million. Production payment applications during 1969 totaled \$2.53 million to principal and \$536 thousand to interest. Engineering projections indicate that the major remaining production payments will be liquidated in 1972.

The Company during 1969 participated in the drilling of seven wells in the Mid-Continent Division. Three wells were completed as oil producers, two as gas producers, plus one water injection well and one water supply well.

The more significant activities undertaken in the Mid-Continent Division are described as follows:

**KANSAS** The Company owns a one-half leasehold interest in oil rights only in 19,360 acres and oil and gas rights below 3,400 feet in 2,640 acres located in Finney, Haskell, Kearny and Seward Counties, Kansas. These counties are located in the western part of the State and overlie a portion of the Upper Limits of the Anadarko Basin where exploratory drilling has been increasingly active during the past several months. Your Company has farmed out several tracts in this area during the year, including the Freeman Lease where a well was drilled resulting in a dually completed well for gas in the Upper Morrow Sand and oil in the Lansing-Kansas City Zones. At the present time, the Company plans to participate in the drilling of a well on its 160-acre Fischer Lease which will be an offset to an excellent gas well in the Upper Morrow Sand.

**NEBRASKA** The Company, as Operator, drilled one development producing well in the Enders Field Unit in which the Company owns a 46.04% interest. One field development well was also drilled which extended the Dietz Field, "J" Sand Reservoir, by one 40-acre location and proved up at least one more location.

**NEW MEXICO** The Company, together with other working interest owners, completed the engineering studies and finalized the documents during the year necessary to effect four unitized secondary recovery projects. It is anticipated that these projects will be effective by mid-year 1970 and the water injection programs initiated prior to year-end. Reserve was elected Operator of two of the projects containing ninety-five (95) and twenty-seven (27) wells; and will own working interests in the four unitized projects ranging from 5.77% to 40.08%. It is estimated that the future oil reserves to the Company's interest in the four unitized projects will be 1,396,400 barrels. The formations to be included in the secondary recovery projects are the Yates, Seven Rivers and Queens. Each of these formations has been subject to successful waterflood projects in the Lea County, New Mexico Area. The most successful project to date is the Langlie-Mattix-Woolworth Unit in which the Company owns a 4.71% interest. During 1969 this unit produced an average of 1539 barrels per day as against a rate of 428 barrels a day at the time of first

significant water injection response in 1966.

**TEXAS** The Company-operated GMK (San Andres) Unit located in Gaines County, Texas, has been operated as a unitized project since March 1, 1968. Initial water injection into the San Andres Reservoir commenced in August, 1968, at which time the oil production averaged 934 barrels per day. During 1969 the reservoir responded to the water injection program with oil production averaging 1,522 barrels per day at year-end. It is anticipated that the oil production rate will continue to increase during 1970

as additional producing wells are affected by the water injection program. The Company's 34.4% average unit interest over the life of the project constitutes one of Reserve's important properties. At year-end, the Company projected future net oil reserves of 3,798,500 barrels to its unit interest which will generate a future net income of \$8,450,000 to the Company over the life of the waterflood program.

During 1968 the Company farmed out its 100% interest in the Katie Mae Kelly (668 Acre) Unit, Gregg County, Texas. Two oil wells have now been completed as producers in the Upper

## Source and Disposition of Funds 1969

### SOURCE OF FUNDS:

Operating revenues, excluding contract receivables . . .	\$42,533,446
Collections on land sales contracts . . . . .	785,102
Less costs and expenses, excluding non-cash charges . .	<u>36,025,872</u>
Cash flow . . . . .	7,292,676
Proceeds from loans, note collections and changes in current portion of receivables and payables . . . .	2,614,765
Proceeds from disposition of assets . . . . .	1,890,672
Working capital decrease . . . . .	998,174
	<u>12,796,287</u>

### DISPOSITION OF FUNDS:

Principal applications to production payments . . . . .	4,213,396
Capital asset additions . . . . .	6,785,278
Note payments and new notes . . . . .	1,107,259
Dividends paid . . . . .	414,791
Investments and merger and stock conversion costs . . .	275,563
	<u>\$12,796,287</u>

## Exploration, Development and Operations, continued

Travis Peak Zones by the Operator. The Company retained a 13.89% gross overriding royalty in this venture.

**WESTERN DIVISION** As a result of the Mohawk acquisition, the Company now owns interests in a number of producing fields and units in Wyoming. These include the Recluse Field, the Burke Ranch Unit, Cottonwood Creek Unit, Desert Springs Gas Unit, South Coyote Creek Turner Sand Unit and Field, Skull Creek Unit, West Desert Springs Field and West Mush Creek Field. The Company also acquired working interests in 154,123 gross acres (134,138 net acres) of exploratory lands located in Wyoming, Utah, California and Colorado.

In the Recluse Field Reserve acquired a 100% working interest in two wells and a 50% working interest in a third well in this relatively new field. The gas production from these flowing wells is subject to State of Wyoming allowable restrictions. Efforts are being made to unitize this field in order to take advantage of the large gas cap and to increase ultimate recovery through water flooding.

**Wilmington Field, California** Reserve participated in drilling or redrilling 25 wells including 4 producing oil wells, 3 water injection wells and 18 water disposal wells. Extensive remedial work was done on existing wells to improve secondary recovery performance. In Fault Block IV, the primary oil production was com-

pletely recovered in October. Upon entering the secondary recovery stage, Reserve's unit participation increased resulting in an additional 80 barrels per day of oil to the Company's interest.

**Tejon Area, California** Four development wells, in which the Company has a 25% interest, were successfully completed in the South Central Tejon Field from the Lower Reserve sand. These wells, Nos. 77A, 86A, 87A and 95A, extended the field to the east and produced at initial rates varying from 44 barrels per day to 205 barrels per day of 21 gravity oil. Additional drilling is scheduled.

**Liberty Island Gas Field, California** In drilling LFR No. 11 as a development well in this field the Company was successful in obtaining its best well in the area. The well was completed in October 1969 at a top structural position with maximum available sand thickness. Initial production was 2.6 million cubic feet of gas per day with no water through a 1/4" orifice at a pressure of 1624 psi.

**Alaska** In July, Reserve through its subsidiary, Halbouty Alaska Oil Company, completed the drilling of the Theodore River No. 1 well, located on the North Shore of the Cook Inlet, Northeast of the Beluga River gas field. The well was drilled to a total depth of 12,025 feet in search for the Beluga River Gas Sands and the Middle Ground Shoal Sands. Total cost of the well exceeded \$1 million. The well was a dry hole and was considered an

adequate test of the objective formations. This test was drilled without cost to your Company.

**Halbouty-Reserve U.S.A. Exploration Program** During 1969 the Program participated in the drilling of 14 new prospects located in Wyoming, Texas and Louisiana, resulting in the discovery of 2 new gas condensate pools and one new oil pool.

In March, the J.B.S. Lalonde No. 1 was completed as the discovery well in the Sparta "A" pool of the Opelousas Field in St. Landry Parish, Louisiana. The well was perforated in the interval 12,144-150 feet and the initial production of the well was 1,165,000 cubic feet of gas per day and 312 barrels of 39 gravity distillate through a 1/8" choke with 6992 psi flowing tubing pressure. Three additional development wells were drilled and completed in this pool during 1969 and a fourth well is currently being tested. The Program owns interests varying from 50% to 88% in these wells, and from 50% to 100% in approximately 4000 acres in the immediate area.

In June, the No. 1 Pan Am Fee was completed as the discovery well in a new pool of the South Bell City Field located in Jefferson Davis Parish, Louisiana. The well was completed in the Cibicides hazardi sand in the interval 11,963-11,967 feet. On initial production the well flowed 2.4 million cubic feet of gas per day and 36 barrels of distillate through a 14/64" choke, with 2561 psi flow-

ing tubing pressure. Open flow potential of the well was calculated at 14 million cubic feet of gas per day. The Program owns interests ranging from 50 to 70% in approximately 1280 acres surrounding the discovery well.

In July, the No. 1 Bible Bruner was completed as a new pool discovery in the Northeast Woodlawn Field in Jefferson Davis Parish, Louisiana. The well was perforated in the interval 9678-9680 feet in the Upper Frio sand. Initial production was 200 barrels of 34 gravity oil per day through a 9/64" choke with 1445 psi flowing tubing pressure. Two additional development wells were drilled and completed and one dry hole was drilled. The Program owns a 50% interest in these wells and 2895 acres surrounding them.

**Reserve-Halbouty Canadian Exploration Program** During 1969 fifteen exploratory wells were drilled and completed under the Reserve-Halbouty Agreement and three wells were drilling or in the process of completion at year-end. One of the completed wells and one of the wells in the process of completion at year-end resulted in new field discoveries.

In August 1969 the Virgo 15-30 well in the Virgo-South Zama area of Northwestern Alberta was completed as a new field discovery from the Keg River Reef formation with an initial potential of 363 barrels per day. At December 31, 1969 the discovery well, located on a 160 acre parcel in which Reserve-Halbouty owns 20%, had produced 72,360 barrels of oil. In



Top—Aerial view of drilling rig completing Halbouty-Reserve No. 2 White, our 6th producer in the South Opelousas Field, St. Landry Parish, Louisiana.

Center—Rig on location during completion of Halbouty-Reserve #2 White.

Bottom—Drilling crew pulling pipe from total depth of 2.4 miles for completion of Halbouty-Reserve #2 White.



Sunset views are spectacular in Northeast British Columbia.

## Exploration, Development and Operations, concluded

this same area the Virgo 6-28 well, at year-end, was in the process of completion as a new field discovery in the Keg River Reef formation, on a 460 acre lease owned 25.6% by Reserve-Halbouty. Subsequent to year-end, the well was potentialed for 360 barrels of oil per day.

Reserve-Halbouty participated in a continuous seismic and drilling program in the Berland River area of Western Alberta in search of prolific gas reserves in the Upper Devonian Woodbend Reef formation. This sedimentary basin area is located on a northern extension of the Strachan-Ricinus Reef trend where large gas reserves have been discovered in 1968 and 1969 and where exploration activity has continued to increase. Reserve-Halbouty owns interests ranging from 5.62 to 30% in 2,720 acres of Crown Leases and two 12,800 acre Drilling Reservations. At year-end, Reserve-Halbouty was a 12% participant in a 14,000 foot exploratory test well drilled on one of the Drilling Reservations as a follow-up to the Berland 3-23 well which established gas reserves in the Wabamun and Beaverhill Lake formations in 1968. A third exploratory Woodbend Reef test well will be drilled beginning in March 1970, on the remaining 12,800 acre Drilling Reservation.

Reserve-Halbouty has completed negotiations on 8 exploration prospects in Alberta to earn varying interests in wildcat lands. These prospects should be drilled in the first half of 1970.



## Company's Net Share Oil and Gas Sales 1969

	Crude Oil and Natural Gas Liquids—Bbls	Dry and Casinghead Gas—Mcf
Texas .....	665,071	6,322,822
California .....	378,939	1,407,702
Wyoming .....	205,664	155,278
Nebraska .....	113,979	—
Louisiana .....	101,640	—
Illinois .....	89,454	—
New Mexico .....	48,992	774,892
Oklahoma .....	30,695	152,304
Saskatchewan .....	1,146,141	73,108
Alberta .....	401,526	5,227,898
British Columbia .....	239,990	362,818
Manitoba .....	109,282	—
All Others .....	11,327	142,476
Totals .....	3,542,700	14,619,298
Average per day .....	9,706	40,053

NOTE: The above tabulation includes production applied to the retirement of production payments.

# Hanford Fertilizer Plant

In June 1965 Reserve completed a plant on a 50-acre site at Hanford, California for the production of liquid anhydrous ammonia, a commercial fertilizer. The cost of the plant and related facilities was \$2,400,000. The operating capacity of the plant is approximately 18,000 tons a year. In 1969 the plant produced 14,812 tons of anhydrous ammonia, of which 12,753 tons were sold. However, the operation of this plant did not prove profitable.

Consequently, about two years ago Reserve, with a view to rendering the plant operation profitable and achieving a more competitive position in the California fertilizer market, commenced a major expansion and conversion program to construct a new dry fertilizer plant for the production of ammonium sulphate and a variety of ammonium phosphate dry fertilizer products. In June 1969 two of the four units of the new dry plant went on stream and have since that time been producing phosphate fertilizers. These two units consist of an ammonium sulphate solutions facility, designed to produce 200 tons a day of ammonium sulphate in a 40% solution, and a 200-ton conventional granulation facility to granulate ammonium phosphate products. The third unit, for the production of phosphoric acid at a designed rate equivalent to 50 tons per day of phosphoric anhydride for internal plant use in the manufacture of various phosphate formulations, has been completed except for operating modifications and

installation of additional equipment currently on order. This unit went on stream in September and has been producing phosphoric acid in adequate quantities to meet current plant requirements for dry fertilizer manufacture.

The fourth unit of the new plant is an additional granulation facility—a fluid bed unit designed to granulate ammonium sulphate directly from the sulphate solutions unit of the plant. This granulation unit represents a new design concept not previously utilized in this type of process and unsuccessful start-up operations to date have demonstrated that design modifications are necessary before the unit can be completed as a fully operative facility. This work is now in progress, and if these design modifications are successful the plant will then be operative.

The initial base cost estimate for the expansion and conversion program was \$2.1 million. Changes in design, modernization of units to increase capacity, addition of the fluid bed granulator, plus additional labor and material charges during construction have resulted in expenditures to date of \$5.6 million.

The plant is currently capable of production at an estimated rate of 25,000 tons yearly, which is substantially less than necessary for profitable operations. Every effort is being made to reach a profitable plateau.



Top—A view of the sixty ton per day anhydrous ammonia plant. In the foreground is the syntheses section of the plant where the hydrogen and nitrogen are combined to form the finished product.

Bottom—A portion of the new facilities for the production of dry granular fertilizers. Center is the carbonation tower, and at left the rotary drum filters, both components of the Merseberg sulphate solutions plant.

# Apple Valley Ranchos

The land development business operated by your Company's Apple Valley Ranchos Division contributed substantially to Reserve's overall financial results in 1969.

This business, located in Southern California in the high desert resort and residential community of Apple Valley, is primarily engaged in the subdivision and sale of property in the Apple Valley area. In addition to its primary operations, Apple Valley Ranchos also owns and operates Roy Rogers' Apple Valley Inn and the Apple Valley Ranchos Water Co.

The combined sales and other revenues generated from these operations exceeded \$5.0 million in 1969. Sales of property, including sales of subdivided property sold for others under exclusive sales agency contracts totaled \$2.6 million in 1969 and compares with \$3.3 million in sales of such property in 1968. The sales of company-owned property amounted to \$2.2 million in 1969 and \$2.3 million in 1968.

In subdividing activity, Apple Valley Ranchos opened for sale the second segment of the Desert Knolls Manor No. 1 subdivision in July 1969. This property, consisting of 158 residential, multiple and commercial parcels with a sales value of \$2.2 million, is located on a hillside close to the picturesque Mojave River Narrows and has a commanding view of the valley, river and the mountains beyond. A second subdivision, Ramona Ranchos No. 3 containing 72 residential parcels with

a sales value of \$400,000, was opened in October 1969. This property is close to the Rancho Verde elementary school and the original Apple Valley village shopping district.

Development in five subdivisions is currently in progress and in a short time will add in excess of 900 parcels to the Company's inventory. One of these units, Kiowa Park No. 6 containing 178 lots, will be opened for sale in the first half of 1970. Your Company continues to hold in excess of 8,000 acres of undeveloped and unencumbered property in the Apple Valley area for future development. It is significant to note that in contrast to many other land development organizations, Apple Valley Ranchos pays for construction of the subdivision improvements, including lot grading, paving of streets, and installation of a water distribution system.

Construction of Cedar Springs Dam and Silverwood Lake located to the south of Apple Valley continued in 1969. This \$25 million project is an important segment of the statewide Feather River Water System which is now over 45% complete. The huge earth and rockfill dam will rise to a height of 215 feet and will impound 78,000 acre feet of water in Silverwood Lake. The lake will cover 988 surface acres and have a shoreline of 13.4 miles. The San Bernardino Tunnel which will carry water from Lake Silverwood to the San Bernardino Valley was "holed-through" Jobs Peak near

Cajon Pass in January 1970. This four mile long tunnel was excavated to a 13 foot diameter and will be completed at a cost of \$21 million in 1971 along with the dam and lake. These facilities will be the center of a \$6.4 million, 4,400 acre recreational development being planned jointly by the Department of Water Resources, State Beaches and Parks Department and the U.S. Forest Service.

Construction on the Mojave Forks Reservoir Dam, an \$8 million flood control project, also progressed in 1969 and is now over 50% complete. This dam is downstream from the larger Cedar Springs Dam and will also be developed for recreational use. These facilities are expected to stimulate the growth and development of the area, to the benefit of your Company's holdings in Apple Valley.

In 1969 a new airport was constructed in Apple Valley by a recently formed county service district. The new \$2.5 million airport includes a 6,500-foot paved runway and a 5,300 square-foot terminal building located on a 410-acre site approximately four miles north of the Apple Valley Inn. The new and larger facility will materially contribute to the progress and growth of Apple Valley.



Top—Newton T. Bass, Chairman of the Board.

Left—Spectacular sunsets are commonplace on the high desert.

Center, above—Year-round golf is a favorite activity in Apple Valley.

Upper right—One of the West's finest resort-hotels, Roy Rogers Apple Valley Inn.

Lower center—Beautiful homes on spacious homesites are featured in Apple Valley.

Lower right—Recreational horseback riding for outdoor enjoyment in the desert.

Bottom—Aerial view showing the Apple Valley Inn (upper), the Company's Apple Valley headquarters building (lower left) and the Security Pacific National Bank and other commercial buildings (lower right).



# Mohawk Petroleum Corporation, Inc.

In a move toward the status of a more fully integrated oil company, on August 22, 1969, Reserve completed the acquisition of Mohawk Petroleum Corporation, one of California's oldest independent oil companies engaged in the exploration, producing, refining and marketing of petroleum and petroleum products.

Mohawk's 33 oil and gas producing properties located in California, Texas, Alabama and Wyoming and its 134,138 net acres of exploratory leases in the U.S. and Canada, along with its portfolio of securities and bank notes, were assigned to Reserve. Its refinery and marketing facilities, including 32 parcels of real estate owned in fee, were transferred to Mohawk Petroleum Corporation, Inc., a new wholly-owned subsidiary of Reserve. Malcolm McDuffie, vice president of Mohawk for 17 years, a director for 6 years and an oil man of 30 years' experience, was appointed president of Mohawk, Inc. All of Mohawk's 300 employees have continued their employment either with Mohawk, Inc. or Reserve, or have been retained through consulting arrangements.

Under a re-alignment of management, operations of the new Company are being directed toward continued increases in profitability, greater efficiency and further development of controlled retail gallonage through expansion of the company's program of installation of retail outlets in Discount Stores, Dairy Drive-Ins and Convenience Food Marts, a rela-

tively new and successful concept of gasoline marketing.

Mohawk has for 38 years owned and operated a refinery at Bakersfield, California, where it produces principally regular and premium gasoline, diesel oil and stove oil. In addition to extensive product storage facilities, the refinery has complete truck loading facilities and a direct connection into a common carrier pipeline through which it ships refined products to Fresno, central hub of the extensive San Joaquin Valley marketing area. The refinery is located on the mainline of a nationwide railroad, and has modern tank car facilities.

During 1969 Mohawk received a license from the Oil Import Administration to import 4,543 B/D of crude and unfinished oils. Mohawk delivered this crude oil at points of importation to a major oil company in exchange for San Joaquin Valley crude oil delivered by pipeline into the refinery. Under long-term contracts with this major oil company and numerous independent producers, Mohawk enjoys a dependable and continuing supply of high quality, light gravity crude oil to charge its distillation units. Inputs of crude oil to the refinery during 1969 totaled 5,709,772 barrels, averaging 15,643 B/D. With its modern Unifiner, Catalytic Platformer, and Ethyl blending facilities, the company manufactures high quality gasolines meeting the most exacting major company specifications, and accordingly is able to supply

its customers with a fully competitive product.

Through its marketing divisions located in Northern, Central and Southern California, the company marketed 84,500,000 gallons of gasoline during 1969, an increase of 8.5% over the prior year. This distribution was accomplished through 183 retail outlets, comprising 134 service stations selling Mohawk branded products, 49 rebrand outlets (customers who market under their own brand name), and approximately 110 commercial customers and large wholesale accounts. In addition, during 1969 the company marketed 35,300,000 gallons of diesel and stove oils to truck operators, farmers, railroads, and other refiners in California.

Through exchange arrangements with other refining companies, products are available to Mohawk at most marketing centers throughout the state at a considerable saving in transportation costs, enabling Mohawk to compete vigorously in the San Francisco, Sacramento and Los Angeles marketing areas.

California remains the largest market for motor gasoline in the nation. It is anticipated that Mohawk, with retail marketing outlets established in 105 cities and communities throughout the state, with its long established and widely accepted trade name and its reputation for supplying top quality products at competitive prices, will continue to grow and prosper in the California market.

Left—Bakersfield Refinery. Platformer piping and stabilizer in foreground with furnace stacks and crude distillation towers in the background.



Top right—Bakersfield Refinery. Laboratory left foreground with boilers, furnaces and processing units paralleling A.T.&S.F. Railroad. Product stock tanks right of center with four butane "bullets" lower right center.

Center right—Mohawk service station located in Southern California. Clean—Modern—Functional.

Bottom right—Another Southern California Mohawk service station ready to serve with courtesy and fine quality products.



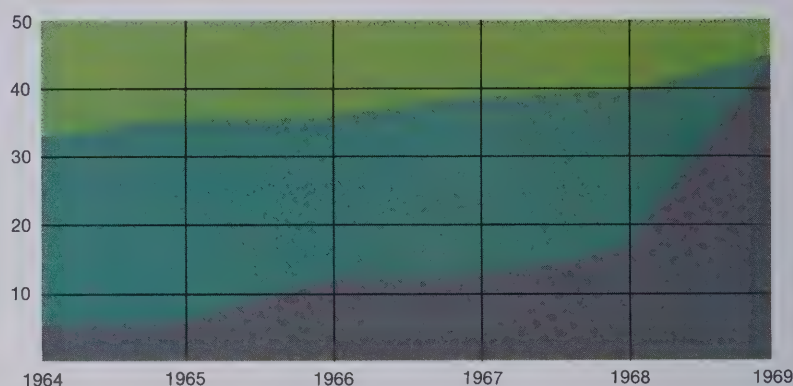
# Financial Review

Consolidated net income amounted to \$4,381,603 in 1969, an improvement of 41.7% over net income of \$3,091,214 in 1968. The figures for both years include the operations of Mohawk Petroleum Corporation accounted for on a pooling-of-interest basis. Net income per common share, based on 8,932,663 average common shares outstanding, amounted to \$.44 in 1969, compared with \$.33 in 1968. Extraordinary item credits included in net income amounted to \$1,422,740 in 1969 and \$333,000 in 1968.

Cash flow totaled \$7,292,676 in 1969. Capital expenditures amounted to \$6,785,278. Working capital at the end of 1969 totaled \$9.2 million compared with \$10.2 million at the end of 1968.

Dividends paid on the Company's four issues of 5½% preferred stock amounted to \$276,041 in 1969. In 1969 capital stock activity, 899,617 shares of Reserve common were issued upon election by holders of the Company's 6½% Convertible Subordinated Debentures which were called for redemption at mid-year. In addition, 974,924 shares of common and 173,790 shares of 5½% cumulative convertible \$25 par value preferred stock were issued in 1969 acquisitions. Employee exercise of stock options, coupled with conversion of preferred stock, accounted for the issuance of 15,907 shares.

(in millions of dollars)

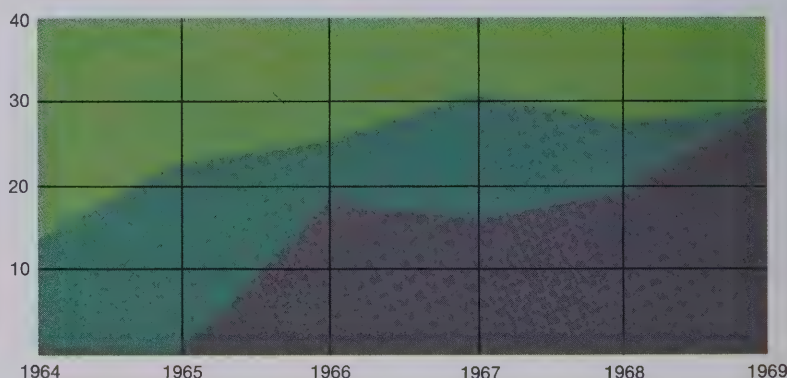


## Revenues

Restated

Originally Reported

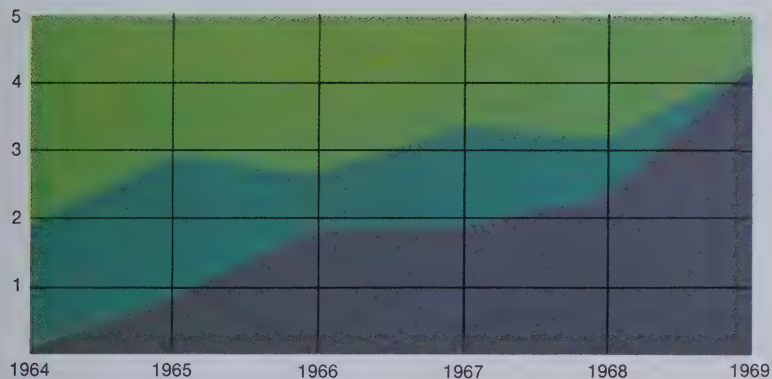
year	originally reported	restated
1964	\$ 5,580,000	\$31,440,000
1965	5,776,000	34,743,000
1966	11,312,000	35,142,000
1967	11,322,000	38,590,000
1968	16,257,000	39,564,000
1969	44,337,000	44,337,000



## Income before Extraordinary Items

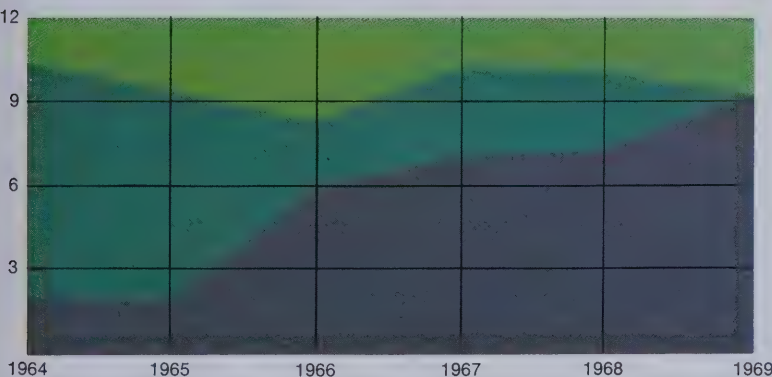
year	originally reported	restated
1964	\$ 48,000	\$ 1,356,000
1965	15,000	2,323,000
1966	1,803,000	2,550,000
1967	1,696,000	3,031,000
1968	1,975,000	2,758,000
1969	2,959,000	2,959,000

(in millions of dollars)



## Net Income

year	originally reported	restated
1964	\$ 211,000	\$ 1,806,000
1965	880,000	2,984,000
1966	1,803,000	2,661,000
1967	1,924,000	3,259,000
1968	2,308,000	3,091,000
1969	4,382,000	4,382,000



## Working Capital

year	originally reported	restated
1964	\$ 2,176,000	\$10,217,000
1965	2,159,000	9,364,000
1966	6,074,000	8,114,000
1967	7,190,000	10,161,000
1968	7,489,000	10,242,000
1969	9,243,000	9,243,000

## Accountants' Report

### ARTHUR YOUNG & COMPANY

CROCKER PLAZA  
POST AT MONTGOMERY  
SAN FRANCISCO, CALIFORNIA 94104

The Board of Directors and Shareholders  
Reserve Oil and Gas Company

We have examined the accompanying consolidated balance sheet of Reserve Oil and Gas Company and subsidiaries at December 31, 1969 and the related consolidated statements of income and shareholders' equity for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances. We have previously made a similar examination of the financial statements for the prior year. We have received the reports of other independent public accountants with respect to their examinations of the financial statements of certain of the Company's subsidiaries for the years ended December 31, 1969 and 1968 whose assets and revenues for 1969 represent 37% and 72% (39% and 69% for 1968) of the respective consolidated totals.

In our opinion, subject to the extent of the future recovery of the Company's investment in the Hanford Fertilizer Plant (see Note 12), and based upon our examination and the reports of other independent public accountants referred to above, the statements mentioned above present fairly the consolidated financial position of Reserve Oil and Gas Company and subsidiaries at December 31, 1969 and December 31, 1968, and the consolidated results of their operations for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis during the two-year period.

March 2, 1970

Arthur Young & Company

# Consolidated Balance Sheet

December 31, 1969-1968

	ASSETS	1969	1968
CURRENT ASSETS:			
Cash—including certificates of deposit, 1968—\$2,727,500 . . . . .		\$ 3,049,114	\$ 6,331,433
Marketable securities, at cost (market value 1969—\$2,584,000, 1968—\$549,406) . . . . .		2,744,049	605,010
Accounts receivable . . . . .		5,944,899	4,274,501
Installment contracts, commissions and notes receivable . . . . .		1,836,831	1,869,131
Inventories, at lower of cost or market . . . . .		3,161,474	3,077,910
Prepaid expenses . . . . .		1,017,813	1,042,549
		<u>17,754,180</u>	<u>17,200,534</u>
INVESTMENTS AND LONG-TERM RECEIVABLES:			
Installment contracts, commissions and notes receivable . . . . .		8,288,326	7,942,600
Investments, at cost, . . . . .		401,946	516,880
Undeveloped land, at cost . . . . .		762,496	744,349
		<u>9,452,768</u>	<u>9,203,829</u>
PROPERTIES:			
Oil and gas properties—gross carrying value . . . . .		75,130,278	74,663,690
Less balance of reserved production payments . . . . .		7,688,853	10,242,566
Oil and gas properties—cost . . . . .		<u>67,441,425</u>	<u>64,421,124</u>
Refining, manufacturing and distributing facilities—cost . . . . .		19,251,578	15,973,545
Commercial and other properties—cost . . . . .		5,548,915	5,412,512
		<u>92,241,918</u>	<u>85,807,181</u>
Less accumulated depletion and depreciation . . . . .		39,441,111	37,543,548
		<u>52,800,807</u>	<u>48,263,633</u>
DEFERRED CHARGE, unamortized debt expense . . . . .		—	419,482
		<u>\$80,007,755</u>	<u>\$75,087,478</u>
LIABILITIES AND SHAREHOLDERS' EQUITY			
CURRENT LIABILITIES:			
Notes payable, current portion . . . . .		\$ 1,000,390	\$ 513,753
Accounts payable and accrued liabilities . . . . .		6,078,618	5,758,307
Exchange oil payable . . . . .		1,237,586	542,918
Federal and state income taxes . . . . .		194,211	144,007
		<u>8,510,805</u>	<u>6,958,985</u>
LONG-TERM LIABILITIES:			
6½ % convertible subordinated debentures due December 15, 1992 . . . . .		—	11,833,000
Notes and other long-term payables . . . . .		4,559,265	2,591,664
Deferred federal, state and foreign income taxes . . . . .		2,476,801	2,037,000
		<u>7,036,066</u>	<u>16,461,664</u>
DEFERRED INCOME:			
Carved out production payments . . . . .		3,385,314	5,044,995
Commissions receivable . . . . .		3,086,951	3,813,856
		<u>6,472,265</u>	<u>8,858,851</u>
SHAREHOLDERS' EQUITY:			
Capital stock			
Convertible preferred stock, \$25 par and involuntary liquidating value: 1969—authorized 400,000 shares; issued 314,203 shares (including 2,435 treasury shares) . . . . .		7,855,075	7,930,500
Common stock, \$1 par value: 1969—authorized 15,000,000 shares; issued 9,325,367 shares (including 3,575 treasury shares); re- served for options, conversion of preferred stock and warrants 1,036,922 shares . . . . .		9,325,367	8,074,843
Capital surplus . . . . .		14,238,302	4,199,572
Earned surplus . . . . .		26,618,520	22,651,708
Treasury stock, at cost, 2,435 shares Series B preferred shares and 3,575 common shares . . . . .		(48,645)	(48,645)
		<u>57,988,619</u>	<u>42,807,978</u>
		<u>\$80,007,755</u>	<u>\$75,087,478</u>

See accompanying notes.

	1969	1968
<b>REVENUES:</b>		
Petroleum products sales . . . . .	\$37,649,512	\$33,651,066
Real estate sales and commission income . . . . .	3,826,712	3,746,577
Interest income . . . . .	702,275	590,128
Other income . . . . .	2,158,022	1,576,631
	<u>44,336,521</u>	<u>39,564,402</u>
<b>COSTS AND EXPENSES:</b>		
Cost of petroleum products sold and operating expenses . . . . .	26,627,424	23,583,701
Cost of real estate sold and provision for loss on reposessions . . . . .	1,030,799	877,540
Selling and administrative expenses . . . . .	7,016,922	5,689,162
Dry hole costs . . . . .	102,989	180,552
Depletion, depreciation and abandonments . . . . .	4,067,650	3,872,961
Interest expense . . . . .	1,537,166	1,866,757
Federal, state and foreign income taxes . . . . .	994,708	735,515
	<u>41,377,658</u>	<u>36,806,188</u>
<b>INCOME BEFORE EXTRAORDINARY ITEMS</b> . . . . .	2,958,863	2,758,214
<b>EXTRAORDINARY ITEMS:</b>		
Federal income tax reduction attributable to loss carryforwards . . . . .	393,000	333,000
Gain on sale of oil and gas properties, less \$594,514 deferred income tax . . . . .	1,029,740	—
	<u>1,422,740</u>	<u>—</u>
<b>NET INCOME</b> . . . . .	<u>\$ 4,381,603</u>	<u>\$ 3,091,214</u>
<b>PER SHARE OF COMMON STOCK:</b>		
Income before extraordinary items . . . . .	\$ .28	\$ .29
Extraordinary items . . . . .	.16	.04
Net income applicable to common stock . . . . .	<u>\$ .44</u>	<u>\$ .33</u>

See accompanying notes.

## Consolidated Statement of Income

Years ended  
December 31, 1969-1968

	Capital Stock Preferred	Capital Stock Common	Capital Surplus	Earned Surplus	Treasury Stock	Total
December 31, 1967 balances . .	\$3,420,775	\$7,201,231	\$ 6,585,212	\$13,950,978	\$(85,983)	\$31,072,213
Mergers . . . . .	4,344,750	639,924	(4,744,488)	5,975,947	—	6,216,133
Preferred stock and debenture conversions . . . . .	(75,025)	172,938	1,988,275	—	—	2,086,188
Stock options exercised . . . . .	—	60,750	411,977	—	—	472,727
Purchase of assets . . . . .	240,000	—	224,850	—	37,338	502,188
Merger expenses . . . . .	—	—	(266,254)	—	—	(266,254)
Net income, 1968 . . . . .	—	—	—	3,091,214	—	3,091,214
Dividends paid . . . . .	—	—	—	(366,431)	—	(366,431)
December 31, 1968 balances . .	7,930,500	8,074,843	4,199,572	22,651,708	(48,645)	42,807,978
Merger . . . . .	—	335,000	(334,861)	—	—	139
Preferred stock and debenture conversions . . . . .	(75,425)	907,334	10,387,165	—	—	11,219,074
Stock options exercised . . . . .	—	8,190	57,298	—	—	65,488
Merger expenses . . . . .	—	—	(70,872)	—	—	(70,872)
Net income, 1969 . . . . .	—	—	—	4,381,603	—	4,381,603
Dividends paid . . . . .	—	—	—	(414,791)	—	(414,791)
December 31, 1969 balances . .	<u>\$7,855,075</u>	<u>\$9,325,367</u>	<u>\$14,238,302</u>	<u>\$26,618,520</u>	<u>\$(48,645)</u>	<u>\$57,988,619</u>

See accompanying notes.

## Consolidated Statement of Shareholders' Equity

Years ended  
December 31, 1969-1968

# Notes to Consolidated Financial Statements December 31, 1969

■ **1. Principles of Consolidation.** The Company's consolidated financial statements include the accounts of all its wholly and majority-owned subsidiaries. The accounts of Canadian subsidiaries have been converted to U.S. dollars at appropriate rates of exchange. Intercompany transactions have been eliminated.

During 1969 the Company issued 974,924 shares of its common stock, 173,790 shares of its Series D convertible preferred stock, and warrants to purchase 100,000 shares of its common stock at \$15 per share in return for the assets, subject to liabilities, of Mohawk Petroleum Corporation and all of the outstanding stock of three Canadian oil and gas corporations, one of which began operations in January 1969. These transactions have been accounted for as poolings-of-interests. Accordingly, the excess of the aggregate par value of the preferred and common stock issued over the aggregate par value of the common stocks of the acquired companies, and the expenses of the acquisitions, have been charged to capital surplus.

■ **2. Installment Contracts, Notes and Commissions Receivable.** Installment contracts, notes and commissions receivable are as follows:

	December 31	
	1969	1968
Installment contracts and notes receivable . . . . .	\$ 7,960,389	\$6,722,032
Less allowance for losses . . . . .	(922,183)	(724,157)
Commissions receivable . . . . .	3,526,951	4,288,856
Less allowance for uncollectible commissions . . . . .	(440,000)	(475,000)
	10,125,157	9,811,731
Portion due within one year . . . . .	1,836,831	1,869,131
Balance due after one year . . . . .	<u>\$ 8,288,326</u>	<u>\$7,942,600</u>

Installment contracts are principally twelve-year notes resulting from land sales, collectible at the rate of 1% per month; these land sales are included in income in the year of sale.

Commissions receivable represent commissions earned on sales of land owned by others. As the Company has no enforceable claim against the purchaser or the original owner of the lot, the receivables are offset in the balance sheet by an equivalent amount of deferred income, to be recognized when collected.

■ **3. Inventories.** Inventories are as follows:

	December 31	
	1969	1968
Petroleum products, at average cost . . . . .	\$1,179,085	\$1,089,707
Fertilizer and chemical products, at lower of cost or market . . . . .	600,733	480,136
Subdivided land, at cost . . . . .	885,033	973,521
Materials and supplies, at or below average cost . . . . .	496,623	534,546
	<u>\$3,161,474</u>	<u>\$3,077,910</u>

■ **4. Properties.** Reserved production payments are added to the cost of the acquired properties. The unpaid balance of the production payments is payable solely out of production from the properties and so is shown as a deduction from the total carry-

ing value. The consolidated statement of income includes proceeds from the sale of production applied to production payments, and related expenses, as follows:

	1969	1968
Petroleum products sales . . . . .	\$ 3,247,000	\$ 3,395,000
Production taxes, depletion and depreciation . . . . .	(1,226,000)	(1,319,000)
Interest expense . . . . .	( 522,000)	( 662,000)
	<u>(1,748,000)</u>	<u>(1,981,000)</u>
Included in net income . . . . .	<u>\$ 1,499,000</u>	<u>\$ 1,414,000</u>

Earned surplus at December 31, 1969 included cumulative earnings thus recorded amounting to \$7,328,000. No provision has been made for related income tax as the Company expects these earnings to be offset by future intangible drilling costs and allowances for percentage depletion.

Depletion and depreciation of the costs of oil properties and related equipment are computed on the unit-of-production basis; buildings and other equipment are depreciated by the straight-line and declining-balance methods at rates varying from 2½% to 33½% per annum.

■ **5. Debentures, Notes and Other Long-Term Payables.** In 1969 the Company issued 899,617 shares of common stock upon conversion of substantially all of its 6½% debentures. Related expenses of \$594,926 (including \$409,236 of unamortized debt expenses) were charged to capital surplus.

At December 31, 1969 the Company had a note payable to a bank for \$4,812,500, (\$187,500 payable quarterly through April 30, 1973, with a final installment of \$2,187,500 due July 31, 1973, with interest payable quarterly at ¼% above the bank's prime rate). The debt agreement requires, among other things, the maintenance of a minimum net worth (as defined), working capital equal to 10% of defined net worth, and prohibits the payment of cash dividends on the Company's common stock.

Other notes and long-term payables include commissions and compensation payable, notes payable, and 5½% debentures payable, of which \$250,390 is due within one year.

■ **6. Federal, State and Foreign Income Taxes.** The liability for deferred federal, state and foreign income taxes represents estimated taxes applicable to installment land and oil and gas lease and permit sales. The Internal Revenue Service has asserted that the Company owes additional tax (with respect to companies acquired by Reserve, for periods prior to acquisition) in the aggregate approximate amount of \$375,000. Reserve is contesting these proposed deficiencies. It is not possible at the present time to estimate what portion, if any, of these amounts will be paid.

Because of its utilization of loss carryforwards, Reserve's federal income tax returns for all years since 1959 are still subject to examination by the Internal Revenue Service.

■ **7. Preferred Stock.** The Company has four series of 5½% cumulative, convertible, voting (except Series C), preferred stock issued and outstanding. Total preferred shares issued at December 31, 1969 are as follows: Series A—25,853, Series B—104,960 (includes 2,435 treasury shares), Series C—9,600, and Series D—173,790, totaling 314,203 shares. Such shares are convertible at



the shareholders' option, into common stock at various rates (subject to anti-dilution adjustments) and are callable by the Company, at its option, at various times and at amounts up to 106% of par value. At December 31, 1969 there were reserved 622,676 shares of the Company's unissued common stock for conversion of the preferred stock.

The remaining 76,121 shares of authorized unissued preferred stock shall have such conversion, dividend and voting rights, and other privileges as the Board of Directors shall designate, if and when such shares are issued.

■ **8. Stock Options.** In prior years, the shareholders approved adoption of a qualified stock-option plan for 50,000 shares of common stock, and a selected employees' stock-option plan for 100,000 shares of common stock. In 1969 the Board of Directors approved, subject to shareholders approval, a qualified stock-option plan for 200,000 shares of common stock. Under the qualified and selected stock-option plans, the Company has granted to certain officers and key employees options to purchase shares of its unissued common stock at the market prices on the dates granted.

During 1969 options as to 136,500 shares were granted at prices ranging from \$8.125 to \$15.375 per share, for a total of \$1,375,812. Options as to 7,250 shares were exercised in 1969 for a total of \$49,844. The market value of these shares at the date of exercise was \$108,906. Options as to 2,000 shares at \$17.75 per share were cancelled in 1969.

At December 31, 1969 options were outstanding on 206,000 shares at prices ranging from \$8.125 to \$17.75 per share for a total of \$2,483,562; options were exercisable at that date as to 69,500 shares for a total of \$1,105,750. The options presently outstanding expire on or before December 23, 1974, if not exercised before that date. At December 31, 1969, 106,000 shares of common stock were reserved for stock options not yet granted.

The Company has a stock-purchase plan for employees of a Canadian subsidiary. During 1969, 940 shares were issued for \$15,644.

■ **9. Warrants.** In 1969 the Company issued, in connection with the acquisition of the stock of a Canadian corporation, warrants to purchase 100,000 shares of its common stock at \$15.00 per share. The warrants expire on September 15, 1974 and may be wholly or partially exercised at any time prior to the expiration date.

■ **10. Net Income Per Share.** Net income per share of common stock is based on the weighted average number of common shares outstanding, and is computed after deduction for dividends paid on the Company's preferred stock. Assuming conversion of outstanding preferred stock and convertible debentures and exercise of outstanding stock options at the beginning of the year, there would have been no dilution of net income per share.

■ **11. Commitments.** A wholly-owned Canadian subsidiary has guaranteed the expenditure of \$1,960,000 for performance of exploration work on Canadian Government oil and gas permits.

■ **12. Hanford Fertilizer Plant.** The extent of recovery of the investment of approximately \$8,000,000 in the Hanford Fertilizer Plant is dependent upon successful resolution of technical production problems and subsequent attainment of its profitable operation.

## Division and Other Offices

### EXECUTIVE OFFICES:

550 South Flower Street, Los Angeles, California 90017

### APPLE VALLEY RANCHOS DIVISION

P. O. Box 1, Apple Valley, California 92307

Walter E. Cramer, Jr., Vice President

### MID-CONTINENT DIVISION

1806 Fidelity Union Tower, Dallas, Texas 75201

Paul D. Meadows, Vice President

### WESTERN DIVISION

Rt. 2, Box 434, Bakersfield, California 93302

Robert P. Mangold, Manager

### FERTILIZER PLANT

P. O. Box 872, Hanford, California 93230

T. S. Melby, Manager

### CANADIAN RESERVE OIL AND GAS LTD.

630 6th Avenue, S.W., Calgary, Alberta, Canada

Paul D. Meadows, President

### MOHAWK PETROLEUM CORPORATION, INC.

900 Wilshire Boulevard—Suite 1100

Los Angeles, California 90017

Malcolm McDuffie, President

## Transfer Agents

### SECURITY PACIFIC NATIONAL BANK

Corporate Trust Division

124 West Fourth Street, Los Angeles, California 90013

### THE CHASE MANHATTAN BANK, N.A.

One Chase Manhattan Plaza, New York, New York 10015

### GUARANTY TRUST COMPANY OF CANADA

311 8th Avenue, S.W., Calgary, Alberta, Canada

and 88 University Avenue, Toronto 1, Ontario, Canada

## Registrars

### THE BANK OF CALIFORNIA, N.A.

550 South Flower Street, Los Angeles, California 90017

### FIRST NATIONAL CITY BANK

55 Wall Street, New York, New York 10005

### GUARANTY TRUST COMPANY OF CANADA

311 8th Avenue, S.W., Calgary, Alberta, Canada

and 88 University Avenue, Toronto 1, Ontario, Canada

## Stock Exchange Listings

American Stock Exchange

Pacific Coast Stock Exchange

Toronto Stock Exchange

